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In the Supreme Court of the United States

OCTOBER TERM, 1991

SAMUELS, KRAMER & COMPANY, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTION PRESENTED

Whether Rule 183(c) of the Tax Court's Rules of Practice and Procedure contravenes 26 U.S.C. 7443A(c).



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OPINIONS BELOW

The opinion of the court of appeals, Pet. App. A1-A42, is reported at 930 F.2d 975. The opinion of the United States Tax Court, Pet. App. A43-A72, is reported at 94 T.C. 549.

JURISDICTION

The judgment of the court of appeals was entered on April 2, 1991. A petition for rehearing was denied on May 14, 1991. Pet. App. A73-A74. The petition for a writ of certiorari was filed on August 8, 1991. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

Like *Freytag v. Commissioner*, 111 S. Ct. 2631 (1991), and some 3,000 other cases that originated in the Tax Court, this case involves a taxpayer who attempted to deduct losses from investments in a commodity tax straddle program operated by First Western Government Securities (First Western). First Western and petitioner were the promoters of that program. The taxpayers in *Freytag* were investors. Pet. App. A45.

The Commissioner of Internal Revenue (Commissioner) disallowed petitioner's deductions, and petitioner filed petitions in the Tax Court seeking redetermination of the resulting deficiencies. The chief judge of the Tax Court assigned petitioner's case to a special trial judge for hearing and report under 26 U.S.C. 7443A(b)(4). Petitioner moved to vacate the assignment on the same grounds urged by the taxpayers in *Freytag*: that a Tax Court special trial judge could not be assigned to hear and report on its case under 26 U.S.C. 7443A(b)(4), and that, if the statute authorized such an assignment, it violated the Appointments Clause, Art. II, § 2, Cl. 2. The Tax Court rejected petitioner's contentions. On interlocutory appeal, the court of appeals affirmed. Pet. App. A1-A42.

1. In 1984, the Commissioner disallowed "loss" deductions claimed by petitioner with respect to its "investments" in First Western. The Commissioner determined the petitioner was liable for income tax deficiencies of approximately \$1.4 million for its 1979, 1980, 1981, and 1982 tax years, an addition to tax of more than \$0.5 million for civil fraud for its 1980 and 1982 tax years, and interest at the penalty rate of 120 percent of the usual rate under 26 U.S.C. 6621 for its

1982 tax year. Petitioner filed petitions in the Tax Court seeking redetermination of those deficiencies. Pet. App. A3-A4; C.A. App. 22, 44, 47.

While petitioner's case was pending in the Tax Court, that court selected several cases (not including petitioner's) to be tried as test cases. After the Tax Court judge to whom those cases were assigned became ill, the test cases were reassigned, with the consent of the parties, to special trial judge Carleton D. Powell for completion of trial and preparation of a report under 26 U.S.C. 7443A(b)(4). After a lengthy trial, special trial judge Powell proposed findings and an opinion in the Commissioner's favor in the test cases. The chief judge of the Tax Court adopted the proposed findings and opinion. *Freytag v. Commissioner*, 111 S. Ct. at 2635.

Several of the test cases were appealed to the United States Court of Appeals for the Fifth Circuit. It affirmed. *Freytag v. Commissioner*, 904 F.2d 1011 (1990).

2. In the meantime, the Tax Court assigned petitioner's case to special trial judge Powell for hearing and report under 26 U.S.C. 7443A(b)(4). Unlike the taxpayers in *Freytag*, petitioner did not consent to the assignment of its case to a special trial judge. Instead, it moved to vacate the order making that assignment on two grounds:

- a. The assignment of a Special Trial Judge to this action exceeds the statutory authority conferred upon Special Trial Judges.
- b. The assignment violates the Appointments Clause of the United States Constitution, Article 2, § 2, cl. 2.

C.A. App. 7, 9.

A division of the Tax Court, in an opinion reviewed by the entire court, denied petitioner's motion. Pet. App. A43-A71. With respect to the statutory argument, the Tax Court held that "the legislative history and structure of section 7443A show that Congress intended to allow the chief judge to assign any proceeding to a special trial judge, provided that a Tax Court judge review the opinion and enter the decision." Pet. App. A51. With respect to the constitutional argument, the Tax Court held that its chief judge was a "Court[] of Law" within the meaning of the Appointments Clause, Art. II, § 2, Cl. 2, and therefore could appoint inferior Officers such as special trial judges. Pet. App. A57-A64. Because of the importance of the foregoing issues for the functioning of the Tax Court, the court certified the statutory and constitutional questions for interlocutory appeal. *Id.* at A71-A72.

The United States Court of Appeals for the Second Circuit granted petitioner's motion for leave to appeal and affirmed.¹ As in the Tax Court, petitioner specified two issues for review:

A. Whether Section 7443A of Title 26, United States Code, authorizes the Chief Judge of the United States Tax Court to appoint a special trial judge to preside over a major tax case involving substantial tax deficiencies and issues of significant importance.

B. Whether the Chief Judge's appointment of a special trial judge to preside over such a major

¹ A similar order was entered in two companion cases, and was certified to the United States Court of Appeals for the Ninth Circuit, but that court denied leave to appeal. *First Western Government Securities v. Commissioner*, No. 90-80125 (May 30, 1990); Pet. C.A. Br. 2.

tax case violates the Appointments Clause of the United States Constitution, Article II, Section 2, Clause 2.

Pet. C.A. Br. 1.

On the statutory issue, the court of appeals agreed with the Tax Court that 26 U.S.C. 7443A(b)(4) authorizes the chief judge to assign any tax case to a special trial judge for hearing and report. Pet. App. A13. On the constitutional issue, the court of appeals agreed that the chief judge's assignment of the special trial judge did not violate the Appointments Clause, Pet. App. A26-A39, but on the ground that the chief judge is the "Head[] of [a] Department," not that he is a "Court[] of Law." Art. II, § 2, Cl. 2.

ARGUMENT

Petitioner contends—for the first time in this Court—that Rule 183(c) of the Tax Court's Rules of Practice and Procedure contravenes 26 U.S.C. 7443A(c). Pet. 9-22. That issue was not pressed before or passed on by either the Tax Court or court of appeals, and therefore is not properly before this Court. Furthermore, resolution of that issue would be premature since Rule 183(c) concerns the scope of the Tax Court's review of a special trial judge's proposed opinion, and the special trial judge has neither heard nor reported on petitioner's case. In any event, Rule 183(c) does not impair the obligation of regular Tax Court judges to make the decision of the Tax Court in cases assigned to special trial judges for hearing and report under 26 U.S.C. 7443A(b)(4).

1. The question that petitioner asks this Court to decide was not pressed before or passed on by the courts below, and therefore is not properly presented. *E.g.*, *Patrick v. Burget*, 486 U.S. 94, 99 n.5 (1988); *EEOC v. FLRA*, 476 U.S. 19, 24 (1986); *Rogers v. Lodge*, 458

U.S. 613, 628 n.10 (1982); *United States v. Lovasco*, 431 U.S. 783, 788 n.7 (1977); *Youakim v. Miller*, 425 U.S. 231, 234 (1976).

In *Freytag v. Commissioner*, 111 S. Ct. 2631 (1991), the first question presented was "Whether a special trial judge of the Tax Court could be assigned to hear and report on petitioners' cases under 26 U.S.C. 7443A(b)(4)." 90-762 Gov't Br. at i. Petitioners in that case sought to go beyond that question and argue that "[e]ven if a special trial judge may hear a complex tax case, he may not effectively resolve it subject only to deferential Tax Court review." 90-762 Pet. Br. at 20. The Commissioner objected that this argument exceeded the Court's grant of certiorari because "[t]he question whether the assignment is permitted is different from the question of the appropriate standard of review once the assignment is made." 90-762 Gov't Br. at 17. This Court agreed with the Commissioner:

Petitioners also argue that the deferential standard with which Tax Court Rule 183 requires a Tax Court judge to review the factual findings of a special trial judge allows the latter not only to hear a case but effectively to resolve it. This point is not relevant to our grant of certiorari, which concerned the question whether the assignment of petitioners' cases to a special trial judge was authorized by 26 U.S.C. § 7443A(b)(4). Accordingly, we say no more about this new argument than to note that under § 7443A(c), a special trial judge has no authority to decide a case assigned under subsection (b)(4).

111 S. Ct. at 2636-2637 n.3.

Like the taxpayers in *Freytag*, petitioner here challenged only the Tax Court chief judge's statutory authority to assign complex tax shelter cases to a spe-

cial trial judge, not the standard of review once the assignment had been completed. Contrary to petitioner's contention, Pet. 4-5, it did not argue in either the Tax Court or the court of appeals that Tax Court Rule 183(c) would effectively allow the special trial judge to decide this case in violation of 26 U.S.C. 7443A(c), and neither court considered that argument. Petitioner referred to Rule 183(c) only to shore up its argument that 26 U.S.C. 7443A(b)(4) did not permit assignment of complex tax shelter cases to special trial judges because such judges in fact decide cases assigned under that provision. See Pet. C.A. Br. 15; Pet. C.A. Reply Br. 5; Pet. Reh'g Pet. 4. Rule 183(c)'s supposed inconsistency with 26 U.S.C. 7443A(c) was not mentioned.

2. It would be premature to determine whether application of Rule 183(c) to this case would violate 26 U.S.C. 7443A(c). As its caption indicates, Rule 183(c) governs "Action on the Report"—i.e., the special trial judge's proposed findings and opinion.² Since this case comes before the Court on an interlocutory appeal of petitioner's motion to vacate the assignment to the special trial judge, consideration of the interplay between Rule 183(c) and 26 U.S.C.

² Rule 183(c) provides:

Cases Involving More Than \$10,000.

(c) *Action on the Report:* The Judge to whom or the Division to which the case is assigned may adopt the Special Trial Judge's report or may modify it or may reject it in whole or in part, or may direct the filing of additional briefs or may receive further evidence or may direct oral argument, or may recommit the report with instructions. Due regard shall be given to the circumstance that the Special Trial Judge had the opportunity to evaluate the credibility of witnesses, and the findings of fact recommended by the Special Trial Judge shall be presumed to be correct.

7443A(c) at this juncture would take place in the absence of any recommended findings, the evidence that might or might not support them, and their bearing, or lack of it, upon a decision, and without knowing the regular Tax Court judge's action in accepting, modifying, rejecting, or recommitting recommended findings, or calling for further evidence with respect to them or to other matters. This Court does not ordinarily consider such anticipatory controversies. Cf. *California Bankers Ass'n v. Shultz*, 416 U.S. 21, 55-57, 72-75 (1974); *Toilet Goods Ass'n v. Gardner*, 387 U.S. 158, 163-164 (1967).

3. In any event, there is no confusion about the responsibility of a regular Tax Court judge in reviewing a special trial judge's proposed findings and opinion in a case assigned under 26 U.S.C. 7443A(b)(4). By statute, a special trial judge has no authority to decide a case assigned under that provision; that remains the responsibility of a regular Tax Court judge. 26 U.S.C. 7443A(c).³ The only court of appeals that has addressed this issue under current Tax Court procedure has concluded that "[t]he chief judge ha[s] both the obligation and power to maintain full responsibility for the decision." *Freytag v. Commissioner*, 904

³ The special trial judge is permitted to make the decision of the Tax Court only in small cases and declaratory judgment proceedings assigned under 26 U.S.C. 7443A(b)(1)-(3):

§ 7443A. Special trial judges

* * * * *

(c) Authority to make court decision

The court may authorize a special trial judge to make the decision of the court with respect to any proceeding described in paragraph (1), (2), or (3) of subsection (b), subject to such conditions and review as the court may provide.

26 U.S.C. 7443A(c).

F.2d at 1015. And this Court—although it did not decide the issue (because the taxpayers did not seek review on that basis, see point 1, *supra*)—signalled its agreement with the court of appeals when it remarked that “a special trial judge has no authority to decide a case assigned under subsection (b)(4).” 111 S. Ct. at 2637 n.3.

Petitioner thinks that Rule 183(c) forbids *de novo* review, and therefore will require that its case be effectively decided by the special trial judge by insulating his proposed findings and opinion from plenary review. Pet. 10. What matters is not what petitioner thinks Rule 183(c) forbids, but what the Tax Court thinks it forbids.⁴ In *Rosenbaum v. Commissioner*, 45 T.C.M. (CCH) 825 (1983), *rev'd sub nom.*, *Stone v. Commissioner*, 865 F.2d 342, 344-347 (D.C. Cir. 1989), the Tax Court held that “the presumptive correctness of the Special Trial Judge’s report does not impair nor dilute our duty of bearing the ultimate responsibility for determining matters before us.” *Rosenbaum*, 45 T.C.M. (CCH) at 827. Although the United States Court of Appeals for the District of Columbia Circuit in *Stone* held that Rule 183(c)’s

⁴ Actually, there is some reason to think that even petitioner could read Rule 183(c) to permit *de novo* review. The taxpayers in *Freytag*—represented by the same counsel who represent petitioner in this case, 904 F.2d at 1011—insisted in the court of appeals in that case that they “are entitled to a careful *de novo* review of the findings of a special trial judge by a tax court judge because the special trial judge cannot make the decision in a case assigned to him under § 7443A(b)(4).” 90-762 Pet. C.A. Reply Br. at 3; *id.* at 3 n.5 (“The responsibility for evaluating the evidence is placed upon the tax court judge who reviews the proposed report of the special trial judge.”); accord 90-762 Pet. Br. at 43 n.42 (petitioners anticipated “*de novo* review * * * when they accepted the mid-trial reassignment to Judge Powell”).

"presumption of correctness" limits Tax Court judges to "clear error" review of special trial judges' proposed factual findings, see 865 F.2d at 345, the Tax Court has never retreated from the position it took in *Rosenbaum*. In accordance with that position, the Tax Court no longer furnishes litigants a copy of the special trial judge's report, nor does it invite the parties to file exceptions to the report. *Ibid.*; *Freytag v. Commissioner*, 904 F.2d at 1015 n.8. As the Fifth Circuit concluded in *Freytag*, "this change in rules, in our view, confirms that the Tax Court's relationship with its special trial judges cannot be analogized to typical appellate review." *Ibid.* No court has held to the contrary since the change in the Tax Court's practice.

The language of Rule 183(c) would not prevent the Tax Court from exercising de novo review. Rule 183 provides that the Tax Court judge responsible for deciding a case may adopt, modify, or reject the special trial judge's report in whole or in part, may request additional briefing, and "may receive further evidence"—an authority that is flatly inconsistent with "clear error" review, under which an appellate tribunal reviews the adequacy of findings on the basis of the record before the fact-finder. See *Anderson v. Bessemer City*, 470 U.S. 564, 573-574 (1985). Petitioner relies entirely on the last sentence in the Rule, which states that "[d]ue regard" shall be given to special trial judges' credibility determinations and that "findings of fact recommended by the Special Trial Judge shall be presumed to be correct." Pet. 9-10. Although the phrasing of this sentence is not ideal, it does not limit the regular Tax Court judge deciding the case to "clear error" review, and has not been so understood by the Tax Court. Instead, the Rule requires the regular judge to start with the facts found by the special trial judge before considering the

parties' proposed findings of "essential fact" under Tax Court Rule 151(e)(3). That interpretation accords with the practice that this Court has established with respect to its Special Masters:

Though the Master's findings on these issues deserve respect and a tacit presumption of correctness, the ultimate responsibility for deciding what are correct findings of fact remains with us. See *Mississippi v. Arkansas*, 415 U.S. 289, 291-292, 294 (1974); C. Wright, A. Miller, & E. Cooper, *Federal Practice and Procedure* §4054, pp. 196-197 (1978).

Colorado v. New Mexico, 467 U.S. 310, 317 (1984). As the Fifth Circuit in *Freytag* correctly concluded, the Tax Court judge to whom the case is assigned "controls the outcome of the case," notwithstanding the presumption of correctness. 904 F.2d at 1015 n.8.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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